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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 684

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

RICHARD J. REYNOLDS

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Fourth Circuit entered in the above cause, reversing the decision of the Board of Tax Appeals.

OPINIONS BELOW

The opinion of the Board of Tax Appeals is reported in 41 B. T. A. 59 (R. 28). The opinion of the court below is reported in 114 F. (2d) 804 (R. 41).

JURISDICTION

The judgment of the court below was entered October 7, 1940 (R. 55). The jurisdiction of this

Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

Pursuant to a testamentary trust established under the will of the taxpayer's father, the taxpayer's share was distributed to him when he became 28 years of age. He thus received not only securities formerly owned by the decedent but also other securities purchased by the trustee. During the year 1934, the taxpayer sold securities of both groups, and the questions presented relate to the proper basis for determining gain or loss upon these sales, namely:

(1) Whether, under Section 113 (a) (5) of the Revenue Act of 1934 and the regulations promulgated thereunder, the basis of the first group of securities is their value at the date of decedent's death, rather than their value at the date of delivery by the trustee to the taxpayer when he became 28 years of age; and

(2) Whether the basis of the second group of securities is their cost to the trustee rather than their value at the date of delivery by the trustee to the taxpayer.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 12–14.

STATEMENT

Taxpayer's father died July 19, 1918 (R. 24). By his will,[1] he provided that the residue of his estate should be divided, one-third to his wife absolutely (with certain qualifications), and the remaining two-thirds "to my children and the living issue of any deceased child, per stirpes, to be equally divided among them, share and share alike," subject, however, to the conditions of a specified trust (R. 16). Under the trust "herein created for the benefit of my children" (R. 17), the trustee was directed to collect "all the income from my children's shares of my estate and, until they severally arrive at the age of twenty-one (21) years, to pay to my wife, out of their respective shares, so much of said income as she may deem necessary or requisite for the support, maintenance, and education of each (of) them" (R. 17). The trustee was given similar discretion in the event that the wife should die before any of the children should become 21 years of age (R. 17). The will then provided (R. 17–18):

[1] For convenience, all references herein to the will are to the extracts therefrom in Exhibit B attached to the taxpayer's petition filed with the Board of Tax Appeals (R. 16). The will is set out in full in Exhibit A, which is referred to in paragraph 3 of the Stipulation of Facts (R. 24). Since Exhibit A is voluminous, it was stipulated by the parties on December 27, 1940 (R. 56) that it need not be printed but that it be separately certified and as such made a part of the record by reference.

(5) From and after each of my said children shall arrive at the age of twenty-one (21) years and until they respectively attain the age of twenty-eight (28) years, said Trustee is authorized and directed to pay to each of them out of his or her respective share of said income, the sum of Five Thousand Dollars ($5,000) per annum, unless, in the opinion of my wife, that amount shall be inadequate to meet the annual requirements of any one or more of my said children. In that event, and at the written request of my said wife, said Trustee is authorized and directed to enlarge said annual payment of Five Thousand Dollars ($5,000) by whatever amount my wife sees fit to designate, provided the total annual allowance does not exceed Fifty Thousand Dollars ($50,000). Should my wife die while any of my children are between the ages of twenty-one (21) and twenty-eight (28) years, then, from and after her death, said Trustee will pay to each of my said children, out of his or her share of my estate, and provided he or she shall have arrived at the age of twenty-one (21) years, Fifty Thousand Dollars ($50,000) per annum, and is directed to accumulate all the balance of said income for his or her respective use and benefit until he or she shall respectively attain the age of twenty-eight (28) years, when each of them shall become entitled to and shall respectively receive from said Trustee his or her share of the corpus of my estate, together with the accumulated income aforesaid.

In the event that any child should die before arriving at the age of 28, such child was in effect given a general testamentary power of appointment over his or her share in the following terms (R. 18):

> (7) Should any of my children die before he or she shall arrive at the age of twenty-eight (28) years, then the share of my estate which would have been payable to him or her, had he or she arrived at that age, shall be continued to be held by my said Trustee for the use and benefit of his or her devisees by Will until the time that such child would have arrived at the age of twenty-eight years, if he or she had lived, when the said trust shall cease and the estate shall then become payable to such devisees, the Trustee, however, paying in the meanwhile the income from said share to them; * * *.

Provision was then made for other disposition in the event of default of exercise of the power of appointment (R. 19).

The trustee received the trust assets from the estate in 1926 and distributed the taxpayer's share, including securities, to him on April 4, 1934, when he became twenty-eight. Some of the securities so distributed had been received by the trustee from the decedent's estate and others had been acquired by the trustee in intermediate transactions. Taxpayer sold some of the securities during the year at a profit. In computing gain, he used as the basis the value on April 4, 1934, when he received them

from the trustee. The Commissioner, however, determined that the proper basis was the value of the securities at the time of the father's death in the case of those then held by the father, and their cost to the trustee in the case of those which it had acquired thereafter (R. 10). The Board of Tax Appeals approved the Commissioner's determination (R. 29), but the Circuit Court of Appeals reversed (R. 55).

SPECIFICATION OF ERRORS TO BE URGED

1. The court below erred in holding that the basis for the determination of the respondent's gain or loss upon the sale by him in the taxable year 1934 of securities which were distributed to a testamentary trustee under the terms of his father's will and by the trustee to the respondent as a part of his share under the will when he became 28 years of age was their value at the date of the distribution to him.

2. The court below erred in holding that the basis for the determination of the respondent's gain or loss upon the sale by him in the same taxable year of securities which were acquired by the trustee in intermediate transactions but were likewise distributed to the respondent by the trustee as a part of the respondent's share under the will when he reached the age aforesaid was their value at the time of their distribution to the respondent aforesaid.

3. The court below erred in holding that, under the terms of the will of the respondent's father, the interest of the respondent in the securities in question was not vested but merely contingent.

4. The court below erred in reversing the decision of the Board of Tax Appeals which had affirmed the Commissioner's determination to the effect that the basis for the determination of the respondent's gain or loss upon the sale by him in the taxable year aforesaid of the securities mentioned in the first specification of error was their value at the time of his father's death and that the basis for the determination of the respondent's gain or loss upon the sale by him in that year of the securities mentioned in the second specification of error was their cost to the trustee.

5. The court below erred in invalidating or failing to give effect to Article 113 (a) (5)–1 of Treasury Regulation 86.

REASONS FOR GRANTING THE WRIT

I

AS TO THE SECURITIES WHICH HAD BEEN OWNED BY THE DECEDENT

1. Section 113 (a) (5) of the Revenue Act of 1934, Appendix, *infra*, p. 12, provides that where property is "acquired by bequest, devise, or inheritance," then "the basis shall be the fair market value of such property at the time of such acquisition." It is not disputed that the tax-

payer had an *interest* in the property immediately after his father's death, but that full enjoyment was postponed until he should become 28 years of age. He also had a general power of appointment over that property which he could exercise by will before reaching that age. Both the taxpayer and the court below apparently recognize that if petitioner's interest were "vested" at the date of his father's death, then that date is the date of "acquisition" within the meaning of Section 113 (a) (5), notwithstanding that actual distribution may be postponed to a later date or may even be defeated by the happening of a condition subsequent. However, the taxpayer contended and the court held that the interest was "contingent" rather than "vested" under North Carolina law, and that therefore the time of acquisition under the statute was the date the contingency was finally resolved—i.e., the date of distribution to him when he became 28 years of age.

The result thus reached below turns upon the illusive distinction between a "contingent" interest on the one hand and a "vested" interest (which may be divested by the identical contingency), on the other hand—a distinction rejected by this Court for estate tax purposes in *Helvering* v. *Hallock*, 309 U. S. 106. The decision below is thus in square conflict with *Van Vranken* v. *Helvering*, decided by the Circuit Court of Appeals for the Second Circuit

on December 2, 1940, not yet officially reported but found in 1940 C. C. H., Vol. 4, par. 9807, as well as with the *per curiam* decision of the same court on the same day in *Archbold* v. *Helvering* and three other cases disposed of therewith, likewise not yet officially reported but found in 1940 C. C. H., Vol. 4, par. 9808.[2]

2. In deciding against the Government, the court below necessarily invalidated applicable Treasury regulations which govern this precise situation. Article 113 (a) (5)–1 (b) of Regulations 86, promulgated under the Revenue Act of 1934, unambiguously provides:

> (b) *Basis.*—Under the law governing wills and the descent and distribution of the property of decedents, all titles to property acquired by bequest, devise, or inheritance relate back to the death of the decedent, even though the interest of him who takes the title was, at the date of death of the decedent, legal, equitable, vested, contingent, general, specific, residual, conditional, executory, or otherwise. Pursuant to this rule of law, section 113 (a) (5) prescribes a single uniform basis rule applicable to all property passing from a decedent by will or under the law governing the descent and distribution of the property of decedents. Accord-

[2] In any event, we do not concede that the taxpayer's interest here was contingent, and we wish to reserve the right to make the contention, as we did in the *Hallock* case, that the taxpayer's interest was vested rather than contingent.

> ingly, the time of acquisition of such property is the death of the decedent, and its basis is the fair market value at the time of the decedent's death, regardless of the time when the taxpayer comes into possession and enjoyment of the property. * * *

Since these provisions have wide application, and since the question is therefore likely to recur frequently, it is a matter of general importance in the administration of the revenue laws that the issue be authoritatively resolved.

II

AS TO THE SECURITIES PURCHASED BY THE TRUSTEE

3. Since the securities purchased by the trustee were not owned by the decedent at the date of death, their basis obviously could not relate back to their value as of the time of death. The Government contended that these securities were not acquired "by bequest, devise, or inheritance" within the meaning of Section 113 (a) (5) of the 1934 Act, and that therefore their basis must be "cost" under Section 113 (a). In rejecting that contention, the decision below is in substantial conflict with *Commissioner* v. *Maguire,* 111 F. (2d) 843 (C. C. A. 7th), certiorari granted October 14, 1940, No. 346, present Term. Although the applicable statutory provision in the *Maguire* case is Section 113 (a) (5) of the Revenue Act of 1928 which establishes different criteria for determining

basis of property acquired from a decedent, the decision is applicable to the extent that it held that securities purchased by a testamentary trustee are not to be treated as acquired by bequest, devise, or inheritance and are therefore to have a basis of cost. In any event, the question is so closely related to the issue in the *Maguire* case that it would be very helpful in the administration of the revenue laws to have the entire matter disposed of by this Court.

CONCLUSION

It is, therefore, respectfully submitted that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

JANUARY 1941.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(5) *Property transmitted at death.*—If the property was acquired by bequest, devise, or inheritance, or by the decedent's estate from the decedent, the basis shall be the fair market value of such property at the time of such acquisition. * * * [U. S. C., Title 26, Sec. 113.]

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 113 (a) (5)–1. BASIS OF PROPERTY ACQUIRED BY BEQUEST, DEVISE, OR INHERITANCE.—(a) *Property included.*—Section 113 (a) (5) applies—

(1) to all property passing from a decedent by his will or under the law governing the descent and distribution of property of decedents; and

(2) to property passing under an instrument which, under section 113 (a) (5) is treated as though it were a will, but applies to such property only at the times and to the extent prescribed in section 113 (a) (5).

(b) *Basis.*—Under the law governing wills and the descent and distribution of the property of decedents, all titles to prop-

erty acquired by bequest, devise, or inheritance relate back to the death of the decedent, even though the interest of him who takes the title was, at the date of death of the decedent, legal, equitable, vested, contingent, general, specific, residual, conditional, executory, or otherwise. Pursuant to this rule of law, section 113 (a) (5) prescribes a single uniform basis rule applicable to all property passing from a decedent by will or under the law governing the descent and distribution of the property of decedents. Accordingly, the time of acquisition of such property is the death of the decedent, and its basis is the fair market value at the time of the decedent's death, regardless of the time when the taxpayer comes into possession and enjoyment of the property. For example, if distribution of personal property left by a decedent is not made until one year after his death, the basis of such property in the hands of the legatee is its fair market value at the time when the decedent died, and not when the legatee actually received the property; or, if the bequest is of the residue to trustees in trust, and the executors do not distribute the residue to such trustees until five years after the death of the decedent, the basis of each piece of property left by the decedent and thus received, in the hands of the trustees, is its fair market value at the time when the decedent dies; or, if the bequest is to trustees in trust to pay to A during his lifetime the income of the property bequeathed, and after his death to distribute such property to the survivors of a class, and upon A's death the property is distributed to the taxpayer as the sole survivor, the basis of such property, in the

hands of the taxpayer, is its fair market value at the time when the decedent died.

The purpose of the Act, in prescribing a single uniform basis rule for property acquired by bequest, devise, or inheritance, is, on the one hand, to tax the gain, in respect of such property, to him who realizes it (without regard to the circumstance that at the death of the decedent it may have been quite uncertain whether the taxpayer would take or gain anything); and, on the other hand, not to recognize as gain any element of value solely from the circumstance that the possession or enjoyment of the taxpayer was postponed. Such postponement may be, for example, until the administration of the decedent's estate is completed, until the period of the possession or enjoyment of another has terminated, or until an uncertain event has happened. It is the increase or decrease in the value of property reflected in a sale or other disposition which Section 113 (a) (5) recognizes as the measure of gain or loss.

* * * * *

(d) *Property acquired before March 1, 1913; reinvestments by fiduciary.*—* * *

If the property is an investment by the fiduciary under a will (as, for example, in the case of a sale by a fiduciary under a will of property transmitted from the decedent, and the reinvestment of the proceeds), the cost or other basis to the fiduciary is taken in lieu of the fair market value at the time when the decedent died.

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